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October 4, 2000

Manager - Dissemination Branch
Information Management and Services Division
Office of Thrift Supervision
1700 G Street NW
Washington, D.C. 20552

ATTN: Docket #2000-57/Mutual Savings Associations, Mutual Holding Company Reorganizations, and Conversions from Mutual to Stock Form

Dear Sirs:

This firm represents several state and federally chartered mutual thrift institutions and is providing comments on their behalf for your consideration. The Office of Thrift Supervision's ("OTS") proposed rulemaking regarding a comprehensive strategy governing mutual institutions, mutual holding company reorganizations and mutual to stock conversions (the "Proposed Rule") is, according to OTS, a method of addressing many concerns that mutual institutions have raised about the OTS's examination and supervision of their business form.

Interestingly, while the OTS hints at providing additional flexibility to mutual institutions in a number of respects, their are few, if any, concrete provisions that will directly affect mutual institutions. Rather, the Proposed Rule requests comment on how the OTS can make it more attractive for mutual institutions to remain in mutual form. For example, while the OTS discusses the potential for mutual capital distributions, no guidelines are provided with respect to whether such distributions will be permissible for mutual institutions. In addition, the OTS requests comment with respect to whether mutual institutions should be permitted to affiliate with other mutual institutions to leverage managerial and administrative resources, and the feasibility of creating banker's banks. Overall, while indicating that a primary motivation for the regulatory revision is in response to mutual institutions' requests for greater flexibility in running their

operations, the OTS provides few, if any, concrete proposals in this area.

The focus of the Proposed Rule is not an effort to benefit mutual institutions, but rather an effort to impose additional OTS oversight on the mutual to stock conversion process, to make it more difficult for management of mutual institutions to make the decision to convert, and to impose an OTS preference for the mutual holding company structure on institutions considering conversions.

We respectfully request that OTS discuss whether there has been a request by any institution, whether in mutual or stock form, to make the specific revisions proposed to the mutual to stock conversion regulations. We doubt whether any mutual or a stock institution requested the revisions which OTS now proposes.

It is clear that healthy mutually chartered institutions cannot, as a practical matter, be forced to convert from mutual to stock form. Rather, that decision is made by management subject to the review and approval of members, after considering a number of factors affecting the future of the institution. Regulations that make it more difficult for mutual institutions to convert through a standard mutual to stock conversion process are clearly not to the benefit of any mutual institution that might be considering conversion. This is the effect of the Proposed Rule. At the same time, the Proposed Rule does not benefit a mutual institution that is not considering such a conversion. The OTS's real reasons for these amendments remain unclear.

One possible reason for the revision is OTS's effort to limit managerial discretion of mutual institutions in making decisions on behalf of their members and their local communities. Presumably, OTS does not trust management to correctly evaluate the benefits of a stock conversion versus the challenges presented by a stock conversion. Rather, the OTS seeks to impose its bureaucratic judgment on such conversions to a much greater extent than is currently the case. We question why this is necessary and whether any institution throughout the country has requested such additional OTS involvement.

More specifically, for well over a decade, the mutual to stock conversion process has been a major factor in revitalizing the thrift industry through offering a methodology for recapitalization

of the industry and permitting the industry, where management deems appropriate, to adopt a stock format that provided benefits in the form of greater ease of combination with other institutions, a means for providing competitive compensation and benefits packages to employees and management, a method for readily taping capital markets and a method for providing for a more direct form of ownership for members.

While the Proposed Rule provides no evidence that any of these benefits have been problematic, the regulatory inference is that standard conversions are likely to be inappropriate for many mutual institutions and that other alternatives should be considered. While such a conclusion may be correct for an individual institution, we believe it is far better to leave that decision to local management and depositors rather than to prejudge the outcome on an industry wide basis through establishment of regulations that will make it far more difficult for institutions to engage in standard conversions.

The Proposed Rule's effect is to limit the options of existing mutual institutions by making it more difficult for them to elect to convert to a stock form in the future.

The Proposed Rule specifically encourages the mutual holding company alternative when considering conversion to stock form. Again, while it may be appropriate for a mutual institution to elect the mutual holding company format, and while it is certainly appropriate for the OTS to consider enhancements to the mutual holding company form to make it more attractive as a long term alternative, the focus of the Proposed Rule is to assert a regulatory preference for mutual holding company conversions. This is entirely inappropriate given the history of stock chartered institutions in this country.

Once again, it appears nonsensical to suggest that mutual institutions "require" an OTS push toward the mutual holding company format. Mutual institutions' management and members can clearly make the determination as to whether they wish to become a mutual holding company, engage in a full stock conversion or remain a mutual institution. That decision should be a local one left to management and depositors. OTS should not be involved in that decision for a healthy institution.

To implement the additional regulatory oversight and impose the regulatory preferences, OTS proposes to require each institution contemplating a conversion to meet with the appropriate regional office to discuss its proposed business plan and receive the non-objection of the regional director before submitting either an application to convert or a notice to reorganize. Such a requirement removes an important management decision from the local board of directors, management and members and places it in the hands of a non-local, regulatory agency. In fact, this additional regulatory intrusion into the process will place an additional chill on management decisions to change their corporate structure.

Under current guidelines, the OTS requires converting institutions to file a business plan in connection with the plan of conversion or reorganization. That business plan is, of course, subject to review by the Office of Thrift Supervision. However, the new requirement for a pre-filing meeting and a formal non-objection prior to commencement of any other portion of the process insures unnecessary delays in the process. The Proposed Rule clearly contemplates that the OTS will advise applicants of whether or not a conversion should go forward.

The Proposed Rule's written standards for an acceptable business plan include requirements for a complete description of the proposed deployment of capital, demonstration of feasibility, discussion of risks and addressing managerial or other resources. It also indicates that the institution's record of success and experience in implementing prior growth or expansion initiatives be discussed.

While these standards address issues appropriate for consideration by the institution, the OTS commentary regarding the proposal makes clear that the OTS will use the provisions to strongly discourage and, if necessary, prohibit well capitalized institutions from engaging in a full mutual to stock conversion. Once again, we don't believe the additional OTS oversight is responsive to any request by current mutual institutions. In fact, we believe virtually all mutual institutions believe that they have adequate managerial ability and board competence to consider the issue of whether a mutual to stock conversion is appropriate. The Proposed Rule's standards suggest that the regulator needs to protect the board and management from making the wrong decision in this area.

In addition, the Regulatory Overview ("Overview") clearly suggests that OTS will discourage institutions that have not previously expanded from converting based upon their lack of success and experience in implementing prior growth and expansion. Of course, the growth opportunities and expansion potential presented by a mutual to stock conversion are without precedent for mutual institutions. The OTS proposed regulation would apparently not permit institutions to convert or, at least strongly discourage them from converting, unless they had already significantly expanded. Such a requirement is ill-advised; the standard should merely be whether an institution has managerial resources required to effectively operate a stock institution and to manage the potential growth opportunities available. Documented experience in implementing prior growth and expansion plans should not be a prerequisite to conversion.

An additional element to the business plan requires demonstration of the ability to realize a reasonable return on equity. The Overview indicates that "at a minimum the projected return on equity should exceed, by a margin reflecting relative investment risk, the institution's rates on long term certificates of deposit. The institution should not consider speculative short term stock price appreciation or the effect of returns of capital or repurchases of stock in assessing the reasonableness of project return on equity, even those may

indeed be factors considered by investors." (Section II.A., Pg. 43094)

The proposed guidelines for preparation of a business plan make long recognized, well established and productive capital management tools such as returns of capital and repurchases of stock unavailable as options available to management to obtain an effective and reasonable return on equity.

We find this portion of the Proposed Rule to be particularly ironic, given the fact that the OTS, in a related and simultaneous rulemaking action, has proposed relaxing stock repurchase limitations that have previously existed for institutions. Under the new OTS guidelines, after the first year following a conversion, specific OTS guidelines regarding the percentage of stock that may be repurchased would no longer apply. However, while the OTS appears to liberalize the stock repurchase rule to permit institution management greater flexibility to run its company, under the new business plan standards, a three-year business plan is required to be filed and followed in detail, and institutions are not permitted to consider the repurchase of stock as part of their capital management for the first three years following conversion.

Thus, the question becomes whether the OTS has indeed liberalized the stock repurchase rule or has merely replaced percentage limitation on repurchases with a business plan limitation for the first three years following conversion. Since the proposal requires that business plans be followed and that any material deviation from an approved business plan obtain prior written approval of the regional director, the overall effect is ongoing OTS management of the institution's capital management strategy for three years following conversion. This appears to be without recent precedent and again suggests that regulators believe they can run an institution's business better than management of the institution.

The Proposed Rule also ignores legitimate business reasons for converting from mutual to stock form other than increasing capital levels. An institution considering a mutual to stock conversion may be well capitalized, and may be deemed to be somewhat over capitalized for a period of time following the conversion. Of course, that institution will need to deploy its capital in an

effective manner following the conversion in order to be fully valued in the market place. However, it has long been recognized that the raising of additional capital is not the only reason for converting from mutual to stock form. Without going into detail, additional reasons include: (i) the ability to attract and retain strong management and employees through stock based compensation plans that permit employees and management to grow with the institution, (ii) the ability of an institution to engage in marketplace transactions such as mergers and other acquisitions which are unavailable to mutual institutions (and, as a practical matter, to mutual holding companies), and (iii) the ability to offer the membership a more direct and recognized form of ownership. Each of these additional reasons has long been recognized by the marketplace (and OTS) as a legitimate reason for conversion from mutual to stock form.

In addition, a fully converted institution, subject to shareholder review and comment, faces an additional level of review of the effectiveness of management of the company. In general, this additional level of review is unavailable to mutually chartered institutions and mutual holding companies through minority public stock holder participation.

It is unclear why the OTS has chosen to ignore these additional reasons for conversion. It is clear that the effect of the Proposed Rule will be for OTS to engage in an additional bureaucratic review respecting the implementation of a three-year business plan following conversion and the imposition of a general bureaucratic determination that well capitalized institutions can demonstrate no meritorious reasons for wishing to convert. We believe each of these developments is unfortunate for the industry, members and management.

The Proposed Rule includes a number of revisions to make the mutual holding company charter more attractive than a full conversion. These revisions include the ability to offer management benefits or stock option plans that permit issuance of more shares than currently permitted and revisions to the waiver of dividend rules. Such revisions are appropriate and would be of benefit to the mutual holding company structure.

However, what is objectionable and unfortunate is the clear intent of OTS in adopting such revisions. This intent is fully

expressed at Section II.H. (pg. 43096) of the Overview when the OTS indicates the "OTS's intent to make the MHC a more suitable, long term alternative to full conversion". Obviously, the OTS revisions are not intended to provide additional options for institutions when considering mutual holding company versus standard conversion, but rather to predetermine that the mutual holding company format is more "suitable" than standard conversions. Once again, this bureaucratic prejudgment by a regulatory agency was not made at the behest of any mutually chartered institution. Mutual institutions can competently make the determination as to whether to adopt a mutual holding company or a full standard conversion structure. They neither need nor desire an OTS predetermination that the mutual holding company structure is more "suitable" than a full conversion.

In addition, the Proposed Rule contemplates a revision of the OTS policy regarding acquisitions following conversion. Under the current regulations and the Proposed Rule, no person or company may acquire more than 10% of any class of equity security of a recently converted institution for three years following conversion without OTS approval. As noted in the overview, the primary purpose of this requirement is to provide a reasonable period of time for the institution to prudently deploy new capital according to the plan described in its offering documents, for the institution to become acclimated as an operating public company and to do both without the distraction of considering takeover proposals.

The Overview notes that, in certain cases, certain groups have approached management shortly following conversion to consider a sale of the institution and, in certain situation, the OTS has approved acquisition of recently converted institutions. The Overview notes that in no event has OTS approved such a proposal before the second year following conversion.

The Overview states OTS's position that acquisitions within the first three years following conversion are not always in the best interest of newly converted institutions, the communities served, or the shareholders. This conclusion is really not subject to dispute, but it is also without much meaning. It is certainly appropriate to state that acquisitions of institutions within three years following conversion are not always appropriate.

However, the OTS reaction to this statement is to now notify the public that it intends to carefully review applications under existing standards to make certain all criteria are fully met before giving written approval of acquisitions within the first three years following conversion. In addition, the commentary notes that "OTS is concerned that even where the acquisition is considered friendly, approval of the acquisition may be inconsistent with the purposes of the existing rules." Sec.II.I. (pg. 43096). Somehow OTS has concluded that because acquisitions within the first three years are not always appropriate, such acquisition must nearly always be inappropriate. The logic does not follow.

We believe a determination as to whether an acquisition proposal is beneficial to an institution is, once again, best left to management and directors of the institution, together with required consideration and approval of the shareholders of that institution. To substitute a blanket OTS inference that acquisitions within three years are not appropriate is without merit and reflects only a cumbersome bureaucratic response to an only dimly perceived problem.

For example, continuation of the current OTS practice of not approving acquisitions within the first year following conversion would appear to be a much more reasonable response. Creation of an artificial regulatory barrier to mergers and acquisitions which may otherwise be beneficial to institutions, depositors and shareholders, is unwarranted.

Once again, the OTS would be hard pressed to note where any institution, whether mutual or stock, has requested an absolute prohibition against acquisitions within three years following conversion. Under the current rules, it is generally understood that an acquisition within three years following conversion that is not favored by existing management and directors of the recently converted institution would be very difficult to complete given current OTS guidelines and currently permitted prohibitions in charters and articles of incorporation under both state and federal law. However, the new guideline seeks to substitute OTS judgement for the judgement of management, directors and shareholders of institutions, somehow assuming that a regulatory judgement in such a matter is more appropriate than that of the owners of the institution. Such a view flies in the face of the ownership

structure established in stock chartered institutions and is not even dimly based on any safety or soundness argument or other operational concern that the OTS might raise.

We believe that this portion of the Proposed Rule should not be implemented and that the current OTS policy which informally refuses to permit acquisitions within the first year following conversion be continued informally or be substituted as a more formal proposition under this portion of the Proposed Rule.

Under Section II.J. of the Overview, the OTS asks whether reorganization into mutual holding companies or mid-tier forms requires the vote of members. The OTS indicates that it is unaware of any reorganization that has failed to receive the majority vote of members and therefore, questions the necessity for expenditure of funds by the institution to obtain such a vote.

Once again, this proposal appears to be an unwarranted regulatory intrusion into the normal approval process for such a major transaction in an institution's life. It may well be the case that reorganization into a mutual holding company form might be opposed by members who feel that the institution might better compete and benefit through remaining a mutual charter or through a full mutual to stock conversion. Thus, we strongly recommend that OTS not eliminate the voting requirement for organization into mutual or mid-tier forms of holding companies, but that such member vote continue to be required so that members may have the opportunity to speak their views regarding such a reorganization.

In summary, we believe that the provisions of the Proposed Rule are problematic in a number of respects as outlined above. We suggest that the OTS reconsider its proposal in light of several factors, including: (i) the absence of any expressed desire for such provisions on the part of either mutual chartered institutions or stock chartered institutions regulated by OTS; (ii) the Proposed Rule's unwarranted imposition and substitution of a broad based, bureaucratic judgement on the best course of action for an institution's future in substitution for decisionmaking by local management, directors and members; (iii) the Proposed Rule's complete lack of concrete provisions seeking to either benefit the mutual institution charter or to make it easier to continue to be a mutual institution; and (iv) the Proposed Rule's unwarranted effort to make full mutual to stock conversions more difficult,

employing a preference for mutual holding companies which is no more than a regulatory preference and which totally ignores benefits to be obtained from a mutual to stock conversion other than the retention of addition capital.

We believe the drafters of the Proposed Rule, and the OTS through its action to implement the Rule, are acting in an unwarranted, unnecessary and overbroad fashion to restrict future mutual to stock conversions. Such decisions are among the most important in the life of a mutual institution, and, contrary to the inference of the Rule, should not be made by non-local regulators, but by the management, board of directors, and members of the institution. The Proposed Rules effort to impose a regulatory preference against mutual to stock conversions and in favor of mutual holding companies and mutual institutions is unwarranted.

No healthy mutual institution has ever been forced to convert against the judgement of its management, directors and members. In fact, the only mutual institutions ever forced to convert have been forced to convert by federal regulators. Thus, to develop a Rule whose central premise is that mutual institutions must be protected against the evils of mutual to stock conversion is totally without merit.

This Rule does not expand the management flexibility of either mutual or stock institutions. It does nothing more or less than to impose the bureaucratic judgement of non-local regulators upon the will of the local management, directors and members of locally-owned and locally-controlled institutions.

We urge the OTS to withdraw the Rule in the areas addressed in our letter and to modify it so as to preserve institutional management control and flexibility to determine the best course of action for institutions. Historically, this has been the approach which works best in the American economic system and, absent significant safety and soundless concerns, it is inappropriate to substitute regulatory judgement for that of ownership judgement.

We appreciate the opportunity to comment upon the Proposed Rule. We urge the staff of the OTS to raise the concerns expressed in this letter directly with those responsible for final approval of the Rule. We believe that if the Proposed Rule is seen in its true light as an effort to substitute regulatory judgement for

ownership judgement, the Rule will be substantially modified since: (1) no mutually chartered or stock chartered OTS institutions has requested such revisions and (2) no safety and soundness or operational concerns are raised by operation of the current conversion rule.

Sincerely yours,

Mallery & Zimmerman, S.C.

Gregory G. Johnson

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